CENTRAL ELECTRICITY REGULATORY COMMISSION
CORE 3, 6TH & 7TH Floor, Scope Complex, Lodhi Road, New Delhi – 110003

PRESS RELEASE

1st September, 2008

CERC proposes rationalization of tariff terms for generation and transmission

The Commission has published draft regulations on terms and conditions of tariff for the period 2009-14 seeking comments of stakeholders by 28th September, 2008. Consumer interests are best served, the Central Commission believes, by ensuring reasonable price for electricity while at the same time facilitating sufficiency of supply through adequate inducements to the investors. The proposed tariff terms announced by the Central Commission bear out this philosophy in letter as well as in spirit. Main highlights are:-

- Tariff fixation procedure simplified. Provision for provisional tariff done away with.
- Benchmarking of capital cost for thermal and transmission projects.
- Post tax ROE of 14% retained.
- Sharing of hydrological risk in a reasonable manner.
- Norms of operation have been tightened .
- Beneficiaries not to take burden of payment of tax on the income on UI earnings and incentives.
- Depreciation rationalized avoiding front loading of tariff.

The regulations reiterate the Commission's commitment to a light handed regulation by providing inter alia for an enabling framework for capital cost benchmarks for prudence check, doing away with the requirement of provisional tariff, benchmark norm for continuous renovation and modernization of plants beyond normative useful life.

The tariff would be determined upfront for the tariff period based on the actually incurred and/or projected expenditure of capital nature and truing up exercise would be undertaken at the terminal year i.e. in 2013-14. Any attempt at over projection is discouraged by providing for refund of excess recovery at SBI PLR rate of interest. This seeks to provide regulatory certainty for the investors while at the same time safeguarding interests of beneficiaries against inflated projection of capital expenditure by the generators and transmission companies.

Capital cost is the starting point for cost plus tariff regulation and the Commission has set in motion a process of controlling such cost through benchmark norms for capital expenditure for thermal generation and transmission projects, proposed to be specified separately. This would go a long way in inducing investors to efficient management of capital expenditure resulting in benefits to the beneficiaries.

The depreciation rates have been rationalized in order to reduce front loading of tariff while at the same ensuring adequate cash flow for the investors. The consumers have also been given relief from payment of tax on the income on net Unscheduled Interchange (UI) earnings and incentives. This would reduce the burden of the beneficiaries.

The new mechanism proposed for additional expenditure on maintaining the efficiency of plants , as they age, will ensure that consumers are not required to pay additional return on capital for the same level of benefits.

Tightening of norms of operation especially raising of availability factor for recovery of fixed cost would also relieve the burden of the beneficiaries significantly. In hydro, as a departure from the existing practice the hydrological risk has been proposed to be shared between the beneficiaries and the generators.

The new proposed tariff norms also ensure that power sector continues to be attract required investments. 14% post tax ROE has been retained . Incentive for performance better than norms has been linked to availability as against the existing practice of payment of incentive based on actual generation (Plant Load Factor). Thermal generating stations will have a option to avail additional compensation in Rs. Lakh/MW per year terms so that the plant owners remain incentivised to maintain the unit availability at a good level even after its useful life. Norms of operation have been rationalized with due regard to the real life operational constraints and factors like vintage etc. O&M norms have been rationalized by duly factoring in the inflation and reasonable compensation for salary hike of employees.

Salient features of the proposed terms and conditions of tariff are summarized below:

- Tariff fixation procedure simplified. Provision for provisional tariff done away with. Upfront fixation of payment based on actually incurred and/or projected expenditure of capital nature and truing up exercise at the terminal year i.e. in 2013-14.
- Benchmarking of capital cost for thermal and transmission projects and prudence check of capital expenditure based on benchmark norms to the extent possible.
- Provision of additional expenditure rationalized. Separate compensation allowance to meet the expenses on additional expenditure on new parts etc. not within the original scope of work ,without disturbing the capital base.
- Post tax ROE of 14% retained. Return in Indian rupees only.
- Sharing of hydrological risk in a reasonable manner.
- Depreciation rates rationalized avoiding front loading of tariff while at the same ensuring adequate cash flow for the investors. Provision for Advance Against Depreciation (AAD) discontinued.
- Inducement to hedge foreign exchange risk exposure to the extent possible.
- O&M norms factored to inflation and reasonable compensation for pay hike for employees.
- Provision for Renovation and Modernisation (R&M) for life extension, with an alternative option to thermal generating stations by way of an additional compensation so that the plant owner remains incentivised to maintain the unit availability at a good level after its useful life.
- Beneficiaries not to take burden of payment of tax on the income on net Unscheduled Interchange (UI) earnings and incentives.

- Norms of operation have been tightened but with due regard to the real life operational constraints and factors like vintage etc. Target availability for recovery of fixed cost has been raised.
- Incentive payment has been linked to plant availability as against the existing practice of payment of incentive based on plant load fact (PLF).
- Norms for new technologies such as supercritical introduced.
- Provision for sharing of CDM benefits.

(Sd/-)

(Alok Kumar)